

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

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CenturyTel, Inc.	:	
and	:	
Gallatin River Communications, LLC	:	
d/b/a/Century Tel of Illinois	:	
	:	<b>Docket No. 08-0645</b>
Joint Application for approval of	:	
reorganization pursuant to	:	
Sections 7-203 and 7-204 and for	:	
other relief.	:	

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**INITIAL BRIEF OF THE  
STAFF OF THE ILLINOIS COMMERCE COMMISSION**

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The Staff of the Illinois Commerce Commission (“Staff”), by and through its counsel, and pursuant to Section 200.830 of the Commission’s Rules of Practice, 83 Ill. Adm. Code 200.830, respectfully submits its Initial Brief in the above-captioned matter.

## **I. Introduction**

### **A. Procedural History**

On November 21, 2008, CenturyTel, Inc. (“CenturyTel”) and Gallatin River Communications LLC d/b/a CenturyTel of Illinois (“Gallatin River”)(“Joint Applicants”) filed a Verified Joint Petition for approval by the Illinois Commerce Commission (“Commission”) of transactions and agreements which result in CenturyTel acquiring by merger the local exchange and interexchange telecommunications operations of Embarq Corporation (“Embarq”). See, generally, Petition. A status hearing was convened on December 17, 2008 at which a schedule for the proceeding was set. Tr. at 5-10. On December 18, 2008, the International Brotherhood of Electrical Workers, Local 21 (“IBEW”) filed a petition to intervene in the matter. See, generally, IBEW Motion to Intervene. On January 12, 2009, the Administrative Law Judge (“ALJ”) granted IBEW’s motion to intervene. Joint Applicants filed direct testimony on November 21, 2008, Staff and IBEW filed direct testimony on January 16, 2009, and Joint Applicants filed reply testimony on February 2, 2009. An evidentiary hearing was convened in the matter on February 4, 2009, and testimony taken and evidence otherwise adduced. This Brief follows.

## **B. Applicable Law**

The following statutes and regulations are germane to this proceeding:

Section 7-203 and 7-204 of the Public Utilities Act, as amended ("Act"), under which, *inter alia*, Joint Applicants petition the Commission for reorganization provides:

No franchise, license, permit or right to own, operate, manage or control any public utility shall be assigned, transferred or leased nor shall any contract or agreement with reference to or affecting any such franchise, license, permit or right be valid or of any force or effect whatsoever, unless such assignment, lease, contract or agreement shall have been approved by the Commission. Such permission shall not be construed to revive or validate any lapsed or invalid franchise, license, permit or right, or to enlarge or add to the powers and privileges contained in the grant of any franchise, license, permit or right, or to waive any forfeiture. 220 ILCS 5/7-203

Section 7-204 provides:

No reorganization shall take place without prior Commission approval. The Commission shall not approve any proposed reorganization if the Commission finds, after notice and hearing, that the reorganization will adversely affect the utility's ability to perform its duties under this Act. In reviewing any proposed reorganization, the Commission must find that:

- (1) the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service;
- (2) the proposed reorganization will not result in the unjustified subsidization of non-utility activities by the utility or its customers;
- (3) costs and facilities are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes;
- (4) the proposed reorganization will not significantly impair the utility's ability to raise necessary capital on reasonable terms or to maintain a reasonable terms or to maintain a reasonable capital structure ;

- (5) the utility will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities;
- (6) the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction;
- (7) the proposed reorganization is not likely to result in any adverse rate impacts on retain customers. 220 ILCS 5/7-204(b).

Additionally, the Commission shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated. 220 ILCS 5/7-204(c).

### **C. Background**

CenturyTel is a publicly-traded company that is the ultimate parent company of Gallatin River. Gallatin River is an incumbent local exchange carrier in Illinois. CenturyTel has entered into an agreement to acquire Embarq through a stock-for-stock transaction. Staff Ex. 1.0, at 2. Therefore, Embarq will become a direct wholly-owned subsidiary of CenturyTel, and Gallatin River will remain a subsidiary of CenturyTel. Staff Ex. 2.0, at 1-2. CenturyTel is a corporation organized under the laws of Louisiana, and is publicly traded on the New York Stock Exchange. Staff Ex. 4.0, at 3. CenturyTel provides telecommunication service to 2.1 million access lines in 25 states. Gallatin is an incumbent local exchange carrier, providing service to approximately 53,000 access lines in 22 exchanges in the State of Illinois. Id.

The Commission approved previous acquisitions under Sections 7-203 and 7-204 involving Joint Applicants. In Docket No. 07-0043, the Commission approved CenturyTel's acquisition of Madison River Communications which resulted in the indirect acquisition of Gallatin River. In Docket No. 06-0683, the Commission approved

a recapitalization transaction involving an Initial Public Offering requested jointly by Madison River and Gallatin River. Staff Ex. 1.0, at 3.

Staff recommends that the Commission resolve reorganization issues as they relate to Section 7-204(b) and 7-204(c) as follows:

## **II. 7-204(b) Issues Presented for Consideration of Reorganization**

### **Issue 1 – Will the proposed reorganization diminish CenturyTel’s ability to provide adequate, reliable, efficient, safe and least-cost public utility service?**

Joint Applicants’ witness G. Clay Bailey states that upon completion of the transaction, end user customers will continue to receive service from the same local operating company and at the same rates, terms and conditions as before the transaction. As such, Mr. Bailey states that the transaction will be transparent to Gallatin’s customers. Joint Applicants Ex. 1.0, at 2. Mr. Bailey refers to Dockets 05-0013 and 06-0683, which were reorganization proceedings arising from planned initial public offerings (“IPOs”) impacting Gallatin, as well as Docket No. 07-0043, Gallatin River’s acquisition by CenturyTel. Relative to Section 7-204 of the PUA, Mr. Bailey notes that Gallatin River remains under conditions or provisions recommended by Staff, and testifies that “...Joint Applicants here are willing voluntarily to continue those provisions for a reasonable period of time following the closing of this merger.” Id. at 4. Staff witness Samuel S. McClerren reviewed Gallatin’s last three quarters of Part 730 reporting and found that they missed only one of the service quality measures over the 9 month period: the metric for out of service greater than 24 hours. However, when averaged over the nine month period, Gallatin’s out of service greater than 24 hours remained above standard. The overall level of service quality provided by Gallatin for

the last 3 quarters has been extremely satisfactory, far exceeding the minimum requirements of Code Part 730. Staff Ex. 4.0, at 4-5.

Additionally, the addendum to Gallatin's annual service quality report from Docket No. 07-0043, for the year ending April 2008, and filed with this Commission on August 4, 2008, indicated that Gallatin's service quality exceeded the standards established in Conditions 5(e) and 5(f) of the Commission's final order in that proceeding, which are more stringent than those established in Code Part 730. Staff Ex. 4.0, at 5.

However, Staff had some concerns about the potential impact the reorganization may have on service quality provided by Gallatin. At least theoretically, any reorganization could negatively impact an existing LEC's service quality. For example, there could be a financial incentive for a parent company to reduce operating budgets or planned levels of investment, or service quality could suffer simply from the strain of integrating different operations support systems. This Commission has demonstrated a strong interest in matters of service quality in previous dockets when the proceeding might provide an economic incentive for a local exchange carrier to reduce levels of service quality. Both of the Illinois Bell alternative regulation plans provide economic incentives to maintain minimum levels of service quality. See, *generally*, *Final Commission Order, Illinois Bell Telephone Company: Petition to Regulate Rates and Charges of Noncompetitive Services Under an Alternative Form of Regulation*, ICC Docket Nos. 92-0448/93-0239 (Consol.), October 11, 1994 (hereafter "Alt. Reg. Order"); *Final Commission Order, Illinois Bell Telephone Company: Application for review of alternative regulation plan / Illinois Bell Telephone Company: Petition to Rebalance*

Illinois Bell Telephone Company's Carrier Access and Network Access Line Rates / Citizens Utility Board and the People of the State of Illinois -vs- Illinois Bell Telephone Company: Verified Complaint for a Reduction in Illinois Bell Telephone Company's Rates and Other Relief, ICC Docket No. 98-0252/0335; 00-0764 (consol.) (December 30, 2002) (hereafter "Alt Reg Review Order").

Mr. McClerren notes that, in other reorganizations, the Commission has ordered special reports to monitor the level of service quality of the resulting entity for some interval of time. Staff Ex. 4.0, at 5-6. Mr. McClerren further observes that, based upon Mr. Bailey's testimony, the Joint Applicants believe that leaving the same provisions in place for some additional time following the closing of this transaction will meet the requirements of Section 204(b)(1). Id; see also Joint Applicants' Ex. 1.0 at 18.

To ensure continuing levels of quality service, Mr. McClerren recommends that the Commission require, as an additional safeguard, a one year extension of Conditions 5(e) and 5(f) from Docket No. 07-0043. Mr. McClerren also recommends extending Conditions 5(e) and 5(f) from Docket 07-0043 for one year from the time of closing of this reorganization. Staff Ex. 4.0, at 6-7. Accordingly, Condition 5(e)(iv) of the final order in Docket 07-0043 would not be operative in this proceeding, as it specifies a two year duration. Id.

Staff's recommended extension is of shorter duration than CenturyTel's two-year reporting requirement in Docket No. 07-0043. However, Staff notes that CenturyTel's ownership of Gallatin River has not led to deteriorating service quality, and concludes that CenturyTel does not merit the same level of scrutiny that Staff gave it in Docket 07-0043. Staff Ex. 4.0, at 7.



Mr. Bailey notes that Staff witnesses have no objections to the proposed Transaction subject to the continuation of the same provisions (subject to Mr. Ostrander's suggested revisions) for a year after the closing of the merger. Joint Applicants are willing to extend those provisions for a reasonable amount of time and agree that one year beyond the closing date of the merger is reasonable. Joint Applicants' Ex. 2.0, at 5.

**Issue 2 - Will the proposed reorganization result in the unjustified subsidization of non-utility activities by CenturyTel or its customers?**

The proposed reorganization of CenturyTel and Gallatin River does not impact the opportunity for the subsidization of non-utility activities of Gallatin River by utility operations. There is no change that will occur that affects the opportunity for Gallatin River to subsidize non-utility activities by the utility operations. In direct testimony, Mr. Bailey testified that neither the Embarq acquisition nor the change in ownership of CenturyTel will result in the unjustified subsidization of non-utility activities by Gallatin River or its customers. Staff Ex. 3.0(R), at 3; see also Joint Applicants' Ex. 1.0, at 18-19.

Gallatin River is subject to the cost allocation requirements of 83 Ill. Adm. Code Part 711, its cost allocation manual, and FCC cost allocation rules. The proposed transaction will not change the existing cost allocation procedures or accounting methods, as testified to by Mr. Bailey. Joint Applicants' Ex. 1.0, at 19. In addition, Gallatin River has agreed to the following conditions from the Order in Docket No. 07-0043 as further evidence of compliance with Section 7-204(b)(2):

1. Commission Staff will be granted access to all books, accounts, records and personnel of CenturyTel, Gallatin River, and all of their utility and non-

utility affiliated sister and subsidiary companies, as well as independent auditor's working papers, to the extent permitted by the rules and policies of the independent auditor;

2. Gallatin River will continue to comply with 83 Ill. Admin. Code 711, Cost Allocation Rules for Large Local Exchange Carriers; and
3. CenturyTel, Gallatin River, and all their utility and non-utility affiliated sister and subsidiary companies will conduct bi-annual internal audits, conducted in odd-numbered years, to test compliance with Section 7-204(b)(2) and 7-204(b)(3). The internal audit report documenting findings, conclusions and recommendations will be submitted to the Manager of Accounting of the Commission by March 31<sup>st</sup> of each even-numbered year and associated working papers will be available to Commission Staff for review.

Staff Ex. 3.0(R) at 3-4.

Mr. Ostrander recommends changes to Condition 3 concerning the frequency of the submission of an internal audit report and to indicate the objective of such audit.

Staff recommends that Condition 3 be revised as follows:

~~CenturyTel, Gallatin River, and all their utility and non-utility affiliated sister and subsidiary companies will conduct an bi-annual internal audits, conducted in odd-numbered years, to test compliance with Section 7-204(b)(2) and 7-204(b)(3). The internal audit report documenting findings, conclusions and recommendations will be submitted to the Manager of Accounting of the Commission by March 31<sup>st</sup> of each even-numbered year and associated working papers will be available to Commission Staff for review.~~

The purpose of the internal audit will be to document the procedures performed and conclusions to determine that cost allocations between regulated and non-regulated activities are in compliance with Gallatin River's cost allocation manual filed with the Commission and that the cost allocation manual is correct and complete.

Staff Ex. 3.0(R), at 3-4.

The rationale for this revision is that the Commission currently requires that internal audits be performed on a routine annual basis to insure that there is no cross subsidization of non-regulated operations by the regulated operations of Illinois public

utilities. Staff Ex. 3.0(R), at 4-5. Without additional rationale as to why it would only be appropriate and necessary to examine this issue every other year, Staff recommends that the internal audit be performed annually. Id. Staff also proposes that the condition indicate the purpose of the internal audit so that there is no ambiguity as to what the internal audit should achieve. Id. The internal audit should document the procedures performed and conclusions to determine that cost allocations between regulated and non-regulated activities are in compliance with Gallatin River's cost allocation manual that is filed with the Commission and that the cost allocation manual is correct and complete. Id.

At the time of filing testimony, Staff had one additional concern, however. Staff Ex. 3.0(R), at 9. Specifically, Gallatin River had not filed a cost allocation manual with the Commission as required by 83 Ill. Adm. Code 711, and further directed by the Commission in the Orders in Docket Nos. 05-0013, 06-0683 and 07-0034 (Joint Applicants' Exhibit 1.01, 1.02, and 1.03, respectively). Id. It was Staff's position that Gallatin River must provide evidence that it has on file with the Commission a cost allocation manual before an order approving the reorganization can be entered.

In his reply testimony, Mr. Bailey agrees to extend the provisions from Docket 07-0043. Additionally, Joint Applicants have no objections to the changes Mr. Ostrander suggests as they are consistent with the way that Joint Applicants have responded to prior audits. Joint Applicants do not object to making the annual audit. Joint Applicants' Ex. 2.0, at 4.

Mr. Bailey also noted that at the time Mr. Ostrander filed his testimony, there was no cost allocation manual on file with the Commission. In response, Gallatin River filed a cost allocation manual.. Joint Applicants' Ex. 2.0, at 4.

**Issue 3 - Are costs and facilities fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by CenturyTel for ratemaking purposes?**

The proposed reorganization of CenturyTel and Gallatin River does not impact the ability of Gallatin River to fairly and reasonably allocate costs and facilities between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes. Staff 3.0(R), at 6; Joint Applicants' Exhibit 1.0, at 18-19. There is no change that will occur that affects the method used by Gallatin River to reasonably allocate costs between utility and non-utility activities. Id. In direct testimony, Mr. Bailey testified that neither the Embarq acquisition nor the change in ownership of CenturyTel will impact the ability of Gallatin River to fairly allocate its costs and facilities between utility and non-utility activities. Id.

The Commission can be assured that Gallatin River will reasonably allocate its costs and facilities because Gallatin River is subject to the cost allocation requirements of 83 Ill. Admin. Code 711, its cost allocation manual, and FCC cost allocation rules. The proposed transaction will not change the existing cost allocation procedures or accounting methods, as testified to by Mr. Bailey (Joint Applicants' Exhibit 1.0, at 18-19). In addition, Gallatin River has agreed to the following conditions from the Order in Docket No. 07-0043 as further evidence of compliance with Section 7-204(b)(3):

1. Commission Staff will be granted access to all books, accounts, records and personnel of CenturyTel, Gallatin River, and all of their utility and non-utility affiliated sister and subsidiary companies, as well as independent

auditor's working papers, to the extent permitted by the rules and policies of the independent auditor;

2. Gallatin River will continue to comply with 83 Ill. Admin. Code 711, Cost Allocation Rules for Large Local Exchange Carriers; and
3. CenturyTel, Gallatin River, and all their utility and non-utility affiliated sister and subsidiary companies will conduct bi-annual internal audits, conducted in odd-numbered years, to test compliance with Section 7-204(b)(2) and 7-204(b)(3). The internal audit report documenting findings, conclusions and recommendations will be submitted to the Manager of Accounting of the Commission by March 31<sup>st</sup> of each even-numbered year and associated working papers will be available to Commission Staff for review.

Staff Ex. 3.0(R), at 7.

Staff recommends changes to Condition 3 concerning the frequency of the submission of an internal audit report and to indicate the objective of such audit. Staff also recommends that Condition 3 be revised as follows:

~~CenturyTel, Gallatin River, and all their utility and non-utility affiliated sister and subsidiary companies will conduct an bi-annual internal audits, conducted in odd-numbered years, to test compliance with Section 7-204(b)(2) and 7-204(b)(3). The internal audit report documenting findings, conclusions and recommendations will be submitted to the Manager of Accounting of the Commission by March 31<sup>st</sup> of each even-numbered year and associated working papers will be available to Commission Staff for review.~~

The purpose of the internal audit will be to document the procedures performed and conclusions to determine that cost allocations between regulated and non-regulated activities are in compliance with Gallatin River's cost allocation manual filed with the Commission and that the cost allocation manual is correct and complete.

Staff Ex. 3.0(R), at 7-8.

The Commission currently requires that internal audits be performed on a routine annual basis to insure that there is no cross subsidization of non-regulated operations by the regulated operations of Illinois public utilities. Staff Ex. 3.0(R), at 8. Without additional rationale as to why it would only be appropriate and necessary to examine

this issue every other year, Staff recommends that the internal audit be performed annually. Id.

Staff also proposes that the condition indicate the purpose of the internal audit so that there is no ambiguity as to what the internal audit should achieve. Staff Ex. 3.0(R), at 8. The internal audit should document the procedures performed and conclusions to determine that cost allocations between regulated and non-regulated activities are in compliance with Gallatin River's cost allocation manual. Id. As noted above, Gallatin has filed a cost allocation manual in response to Staff's testimony.

**Issue 4 - Will the proposed reorganization significantly impair Gallatin River's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure?**

Staff believes that the proposed reorganization will not significantly impair Gallatin River's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure. Staff Ex. 2.0, at 2.

According to Janis Freetly, Staff Financial Analyst, Gallatin River currently generates sufficient cash internally to support its operations and forecasts that it will not need to raise external capital in the years 2009 through 2013. Staff Ex. 2.0, at 2-3. Furthermore, Ms. Freetly notes Petitioners' statement that under the current corporate structure, CenturyTel would raise external capital for Gallatin River should the need arise, and that this practice would continue after the reorganization. CenturyTel currently has an investment grade issuer credit rating of BBB- from Standard & Poor's ("S&P") and a reasonable capital structure of 51% debt and 49% equity. Id. at 3. Embarq also maintains an investment grade issuer credit rating of BBB- from S&P. Id.

S&P does not expect the combined company to have a materially-different business or financial risk profile than those of the two stand-alone companies. Id. After the proposed reorganization, CenturyTel's capital structure would comprise approximately 53% debt and 47% equity. Id. The proposed reorganization would not affect the capital structure of Gallatin River. Id. Thus, the proposed reorganization would not significantly impair Gallatin River's ability to raise necessary capital on reasonable terms. Id.

In addition, the Joint Applicants have agreed that: 1) Gallatin River shall pay no dividends unless it meets a majority of certain service quality standards specified in subpart (i) to Condition (e) described on page 20 of Joint Applicant's Exhibit 1.03 and discussed in the testimony of Mr. McClerren; and 2) Gallatin River will have exclusive access to the higher of \$4 million or the currently approved capital expenditure budget, as specified in Condition (f) on pages 20 and 21 of Joint Applicant's Exhibit 1.03. Staff Ex. 2.0, at 3. These conditions ensure that the financial needs of Gallatin River's parents, direct and indirect, will be subordinate to those of Gallatin River. Ms. Freely recommends that, with the imposition of Conditions (e) and (f) for a one year period as recommended by Mr. McClerren, the proposed reorganization will not significantly impair Gallatin River's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure. Id. at 3-4.

In his reply testimony, Mr. Bailey agrees to Conditions (e) and (f) for a one year period to remove any residual concern by Staff. Joint Applicants' Ex. 2.0, at 3. With this agreement, Staff has no further concerns.

**Issue 5 - Will CenturyTel remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities?**



Staff notes that Mr. Bailey specifically acknowledged that the Joint Applicants will remain subject to all applicable laws, regulations, rules, decisions, and policies governing the regulation of Illinois incumbent local exchange carriers. See, generally Joint Applicants' Ex. 1.0, at 21; Staff Ex. 1.0, at 4.

**Issue 6 - Will the proposed reorganization be likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction?**

Staff witness Karen Chang states that in her opinion, there will be no adverse implication to market competition at all. Staff Ex. 1.0, at 4. As Mr. Bailey states, the acquisition of the telecommunications operations in other states will have no impact on competition in the telecommunications markets for which the Commission has jurisdiction in the areas that are served by Gallatin River. Id. at 4-5. Gallatin River has several interconnection agreements in place, and these agreements will not be affected by the reorganization. Id.

**Issue 7 - Will the proposed reorganization be likely to result in any adverse rate impacts on retain customers?**

Mr. Bailey specifically acknowledged that nothing in the proposed reorganization will result in any increase in the rates that Gallatin River charges its retail customers. Joint Applicant's Ex. 1.0 at 22. Moreover, Joint Applicants agree to Condition 4, which would prohibit Gallatin River from increasing any of its tariffed retail rates for noncompetitive services for one year after closing on the acquisition, giving Gallatin River's retail customers further assurance that the proposed reorganization is not likely to result in adverse rate impacts. Staff Ex. 1.0, at 5. Based upon Mr. Bailey's representation, and upon Joint Applicants' acceptance of Condition 4, it is Staff's

opinion that the requirements of Section 7-204(b)(7) are satisfied. Id. According to Mr. Bailey, the Joint Applicants believe that leaving the same provisions in place for some additional time following the closing of this transaction should abate any concern about whether this transaction meets the requirements of Section 7-204(b). Joint Applicant's Ex. 1.0, at 11. In Staff's opinion, leaving in effect the same provisions established in 07-0043 will ensure that the requirements of Section 7-204(b) are met. Staff Ex. 1.0, at 6. It is also Ms. Chang's recommendation, and that of other Staff witnesses, that all the remaining provisions be extended for one year from the day this transaction is finalized. Id.

In his reply testimony, Mr. Bailey agrees that extending the provisions of Docket No. 07-0043 or one year beyond the closing of the merger between CenturyTel and Embarq is reasonable extension and agrees to the extension. Joint Applicants' Ex. 2.0, at 2.

### **III. 7-204(c) Issues Presented for Consideration of Reorganization**

Mr. Bailey testified that there are no savings anticipated by Gallatin River from its regulated intrastate operations as a result of the reorganization. Joint Applicants' Exhibit 1.0, at 23. Mr. Bailey testified that the Joint Applicants are not seeking in this proceeding, nor will they seek in any other proceeding, to recover any costs Gallatin River may incur in accomplishing the proposed reorganization Id. Staff recommends that the Commission rule that: (1) the allocation of any savings resulting from the proposed reorganization would flow through to the costs associated with the regulated

intrastate operations for consideration in setting rates by the Commission; and (2) the Joint Applicants will not be allowed to recover any costs incurred in accomplishing the proposed reorganization in future rate proceedings. Staff Ex. 3.0(R), at 9-10.

In regards to Commission compliance with Section 7-204(c), Staff recommends that the Commission rule that:

- 1) The allocation of any savings resulting from the proposed reorganization would flow through to the costs associated with the regulated intrastate operations for consideration in setting rates by the Commission; and
- 2) The Joint Applicants will not be allowed to recover any costs incurred in accomplishing the proposed reorganization in future rate proceedings.

Staff Ex. 3.0(R), at 10-11.

Staff also recommends that the order in this proceeding clarify that the internal audit reporting requirements agreed to by Gallatin River in Dockets No. 05-0013, 06-0683 and 07-0043 have been superseded by the above internal audit reporting requirement. Id. at 11.

In his reply testimony, Mr. Bailey agrees with Staff's position on Section 7-204(c) in that it is consistent with Joint Applicants' expectation that both merger savings and the costs to obtain those savings created by the proposed Transaction will occur at the holding company level and will not directly impact Gallatin River in the foreseeable future. Joint Applicants' Ex. 2.0, at 4-5. Joint Applicants agree not to seek to recover any of those costs in any future rate proceedings. Id.

#### **IV. Conclusion**

Staff recommends that the Commission approve Joint Applicants' Petition for Reorganization under Sections 7-203 and 7-204.

WHEREFORE, the Staff of the Illinois Commerce Commission respectfully requests that its recommendations be adopted in their entirety consistent with the arguments set forth herein.

Respectfully submitted,

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